EXHIBIT 7

Vulture investors buy up distressed mortgages

Carolyn Said, Chronicle Staff Writer
Published 4:00 a.m., Monday, June 7, 2010

Want a read on the housing market's future?

Ask a vulture investor.

So-called vultures - also known as distressed-asset investors - make money by buying distressed assets, such as soured mortgage loans, and predicting which way the wind will blow to decide when to liquidate.

That means Jon Daurio's economic calculations provide as good a guide as any.

As CEO of Kondaur Capital Corp., which buys thousands of distressed mortgages at a discount and rehabilitates them for resale, Daurio tries to flip those mortgages as quickly as possible.

He has no desire to buy and hold, because he thinks homes are worth less and less as time goes by.

"I think housing prices nationally will drop 10 to 20 percent over the next three years," he said. "We aim to be in and out of the loan in six months."

Since its 2007 founding, Kondaur has grown to have $1 billion in capital, nearly 500 asset managers and a portfolio of about 4,000 loans at any given time. Daurio said it is profitable, but declined to give specifics.

"We are the nation's largest and most frequent buyer of nonperforming loans secured by one- to four-family residences," he said.

The Orange County company exemplifies an emerging class of investors seeking to make a profit from the real estate meltdown, from mom-and-pop speculators snapping up individual foreclosed homes for cash, to mid-size syndicates buying dozens of foreclosed homes to rent out until the market turns, to giant concerns like Kondaur.

Kondaur's business model provides a right-now snapshot of some pertinent real estate fundamentals.

What it buys

Daurio refers to Kondaur's acquisition targets as "scratch-and-dent mortgages." That means home loans that are delinquent, usually by six months or more.

It buys in bulk, often several hundred loans at a time. The sellers are banks, other distressed-asset investors and Wall Street firms that prefer to quickly unload the troubled loans rather than having to foreclose or modify them. "Banks are hideously understaffed" to manage the loans themselves, Daurio said.

In recent months, Daurio has seen an increase in the number of distressed loans for sale.

"Banks are profitable again, so they can afford to take the losses to get these scratch-and-dent losses off their books," he said. "Banks now are being truthful about the value of these loans because they can afford to take the hits."

About $10 billion worth of distressed mortgages hit the market in the first quarter, he said, more than he'd seen at any one time during the previous couple of years.

He pays about 70 percent of the value of the underlying home. For instance, he'd pay $210,000 to buy a $400,000 mortgage on a home now worth $300,000. Obviously, that means the seller is taking a huge loss. Figuring out the homes' values involves a proprietary formula, and takes into account demographic and sociologic data, as well as price opinions from local real estate brokers.

About a quarter of the loans were previously modified by banks to make them more affordable, but the homeowners couldn't make the revised payments and redefaulted.

The greatest share of its mortgages are in Florida and California, followed by the Rust Belt states of Michigan, Ohio, Illinois and Indiana.

How it 'fixes' them

About 80 percent of the time Kondaur takes back title to houses, usually by paying the delinquent homeowners to sign them over as a deed in lieu of foreclosure, but also by foreclosing itself if that is more expedient.

"If I'm right that prices will keep dropping, getting that property today (as opposed to down the road) is worth a great deal," he said.

Its asset managers then find local contractors to rehab the houses and local real estate agents to sell them. It puts the houses in turn-key condition - ready to move in - and tries to have them sold within 30 days of hitting the market.

About 10 percent of the time, it will sell individual loans "as is." The remaining 10 percent of the time it will modify payments to keep the current homeowner in place. He's not enthusiastic about that approach.

"Our experience is that modified loans are worth considerably less than what would be left if the house were foreclosed," he said.

He's clear that he's not running a charity. Told of a Clovis (Fresno County) couple whose home was foreclosed upon by Kondaur last month, he said: "They should have bought a house they could afford."